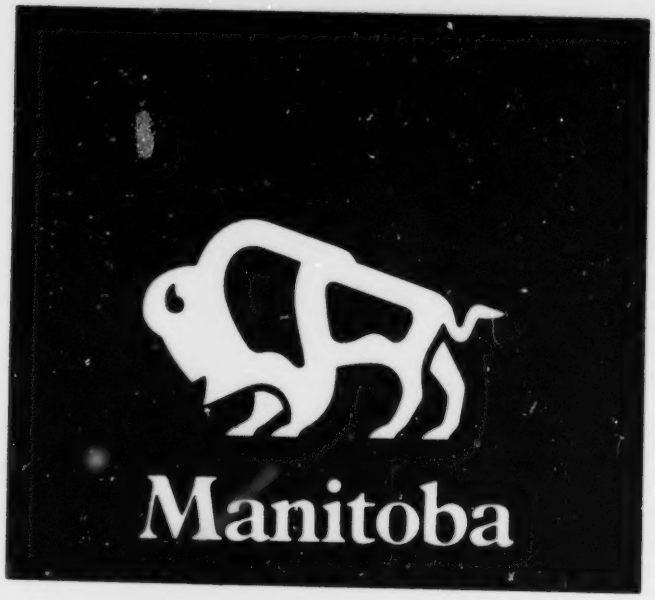

Manitoba's position on:

Federal-Provincial Fiscal Arrangements

Hon. Howard Pawley
Premier of Manitoba

Annual Conference of First Ministers
Halifax, Nova Scotia:
November 28-29, 1985

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MANITOBA POSITION PAPER ON:

FISCAL ARRANGEMENTS FOR HEALTH AND HIGHER EDUCATION PROGRAMS

Honourable Howard Pawley
Premier of Manitoba

Annual Conference of First Ministers
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MANITOBA'S POSITION ON HEALTH AND HIGHER EDUCATION FINANCING AND EQUALIZATION

A SUMMARY

General

The Government of Manitoba believes that adequate and stable federal transfer arrangements are necessary for the economic health of Canada and all its regions, for maintaining essential programs which lie within the constitutional responsibility of provinces, and for sharing the burden of those programs fairly amongst all Canadians.

The Government of Manitoba believes firmly in the process of cooperation, consultation, negotiation, and agreement with the federal and other provincial governments. Unilateral actions, which are usually based on one-sided or one-dimensional reasoning, must be avoided.

Financing Health and Post-Secondary Education

Health and post-secondary education requirements, driven by changes in the age of the population, by technological changes and by new societal demands, will increase as a proportion of Gross National Product. This phenomenom is not restricted or unique to Canada. In the United States, for example, the Conference Board forecasts the costs of meeting health care needs to increase from 10% of GNP in 1981 to 12% by 1990, largely because of the ageing population.

Our public health care system provides comprehensive, quality health programs, universally available to all Canadians, at a reasonable cost. In 1981, some 8% of Canada's GNP was devoted to health care, a significant sum but much more modest than in the United States, where 10% of GNP was allocated to health care.

The Government of Manitoba believes that preserving and improving Medicare and other public health and post-secondary education services to meet the growing needs of all Canadians is preferable to the alternative of reduced public programs and growing private delivery which is expensive, duplicative and inequitable with access to services oftentimes dependent on one's ability to pay for the service.

Health and post-secondary education services will require a slowly growing share of our Gross

National Product to meet the needs of Canadians. Fair federal sharing in these increasing costs is essential.

Under the current funding formula, the federal commitment is virtually frozen in relation to GNP. Thus, unless strengthened, federal support will simply not provide adequate resources to preserve these services for Canadians. The federal share of overall program costs has already dropped from 50% in 1979/80 to 43% in 1984/85. The federal Budget proposal to cut $2 billion from its support, thereby reducing the federal commitment in relation to GNP, is clearly inconsistent with meeting program needs which are growing faster than GNP.

Cuts in federal support are a serious threat to the future of Medicare as we know it. The cuts should not and need not occur.

The federal government must again become an equal partner in financing these services. That would be fully consistent with the Prime Minister's commitment to preserving social programs, including Medicare, as a "sacred trust." It would be consistent with his recognition that the former federal government had "reneged on its share of the costs to provinces" and his advocacy of a return to the "founding principle" of 50/50 cost-sharing.

Equalization

Equalization has often been described as the "glue that holds Confederation together." Certainly, equalization is crucial to the ability of recipient provinces to devote required resources to economic improvements and public services while maintaining competitive tax levels.

In recognition of its importance, the 1982 Constitutional revisions incorporated the principle of equalization and its stated objective:

> "That provincial governments have sufficient revenues to provide reasonably comparable public services at reasonably comparable levels of taxation."

In 1982, the former federal government unilterally changed the basis for calculating equalization support for the six recipient provinces. Among the changes was the lowering of the benchmark or standard of equalization from the all-province national average to the so-called "representative average" which used five-provinces, British Columbia, Saskatchewan, Manitoba, Ontario and Quebec, as the standard.

Under this standard, equalization support is inadequate to raise the recipient provinces to the national average. Currently, the shortfall is close to $1,000 for each family of four in recipient provinces. That in turn has a significant impact on their ability to provide comparable services with comparable taxes.

It should be no surprise that since 1982, the equalization arrangement has required an ongoing series of temporary fixes, patch-ups and overrides to produce at least minimally acceptable results from the perspective of the federal government. These included transition arrangements, special provisions in Atlantic off-shore resource revenue sharing arrangements, floor provisions and supplementary payments. Not withstanding these special provisions, as various observers such as Tom Courchene, the Macdonald Royal Commission and former federal Finance Deputy Marshall Cohen have pointed out, Manitoba was "hardest hit" by the 1982 changes.

Though equalization payments are not a substitute for adequate and fair federal support for health and post-secondary education and other cost-shared services, the spectre of cuts in federal support in vital program areas makes basing equalization on the all-province national average standard even more critical. Otherwise, services in recipient provinces are doubly threatened with poorer provinces requiring larger tax increases than richer provinces to maintain services.

Manitoba's position continues to be as it was in 1982, -- equalization should be based on raising recipient provinces' ability to generate revenues to the all-province national average standard. In our view, that standard best reflects the constitutional commitment and the purpose of the Equalization Program.

NOTES FOR A STATEMENT
ON FEDERAL-PROVINCIAL ARRANGEMENTS FOR FINANCING HEALTH AND POST-SECONDARY EDUCATION

HON. V. SCHROEDER
MINISTER OF FINANCE
GOVERNMENT OF MANITOBA

FEDERAL-PROVINCIAL CONFERENCE
OF FINANCE MINISTERS AND PROVINCIAL TREASURERS

TORONTO, ONTARIO
NOVEMBER 6, 1985

Introduction

Just over one year ago, the people of Canada gave a new federal government a strong mandate to fulfill major promises, promises which included:

1. bringing in a new era of federal-provincial cooperation; and

2. preserving and enhancing national social programs, including Medicare, as part of the "sacred trust."

There was also a commitment to reducing the federal deficit with explicit assurances that that would not be accomplished by cutting vital programs or services directly or through the back door route of offloading responsibilities onto the provinces.

Now, just under fifteen months later, we are meeting to discuss federal proposals for cuts in the federal commitment to health and post-secondary education programs throughout the country. When we met one month ago to begin consultations on the future of health and post-secondary financing for the 1987/88, to 1991/92 period, provinces were informed that Ottawa was considering commencing major cuts next April, a full year before the expiry of the current five year funding formula.

While I fully expect Ottawa will not proceed with cuts in health and higher education support next April, and will instead provide time for meaningful consultations, the proposal to begin cuts a year early has detracted from the atmosphere of constructive cooperation in federal-provincial relations which all governments would like.

Of more fundamental importance to all Canadians is the impact federal cuts have for the future of our public health care and higher education systems.

Trends in Federal-Provincial Cost-Sharing

Recently, I released a Background Paper on the federal-provincial arrangements for funding health and post-secondary education programs. The document included summary data on health and higher education

spending in the ten provinces based on information provided by all provinces and coordinated by Ontario officials. I would like to thank Ontario for its efforts in this regard.

The trends in expenditures and in federal support are clearly evident from the summary data.

1. Expenditures on Health and Post-Secondary Education are large and growing faster than other provincial program expenditures and faster than the rate of growth in the economy. In 1984/85 some $33.9 billion was devoted to these programs in the ten provinces.

2. Federal support under the Established Programs Financing Arrangements for health and post-secondary education are by far the largest of the federal transfer payments to provinces. In part due to unilateral federal cutbacks initiated by the former federal government, the federal share of program financing for health and post-secondary education has fallen from 50% in 1979/80 to 43% in 1984/85. Federal support fell some $2.4 billion short of a 50% share in overall program costs.

Over the years, there have been many irritants inflicted on federal-provincial relations. However, in my view, among the most serious affecting provincial relations with the previous federal government were:

- the frequent recourse to unilateral action rather than the alternative of consultation, negotiation and finally agreement; and

- the pressures placed on provincial finances because of reduced federal support for programs in which an equal federal-provincial partnership was clearly needed.

With a new federal government in Ottawa committed to federal-provincial cooperation, our Government looked forward with some optimism to a fair sharing of costs and responsibilities for vital services. In health and higher education, we hoped that the key principles of adequacy, stability and flexibility, would be honoured.

Our Government and others are willing to sit down and discuss these important issues with the federal government. Because of the importance of the discussions to health and education services, I believe our discussions should include our respective Health and Education Ministers.

The Threat to Public Health and Post-Secondary Education Programs

Recently, the Conference Board projected that health costs in the United States will grow from 10% of GNP in 1981 to 12% in 1990 in large part because of the increased costs of providing care for the rapidly increasing number of elderly people. Our Canadian system has proven remarkably adept at meeting health care needs at moderate costs. In 1965, both the U.S. and Canada spent about 6% of their GNP on health care. But with the efficiencies of our public health care system, the proportion of GNP devoted to health care by Canadians had grown to only 8% by 1981 compared with 10% in the U.S.

Nevertheless, despite our efficiencies, we face much the same demand pressures -- meeting the health care requirements for an ageing population, new health technologies, and so on -- that are at play in the U.S. As the Macdonald Commission noted, by 1990, Canada will have fully one-third more senior citizens than in 1981. I do not believe our already efficient but strained health care system will be able to serve these people without increasing its call on the nation's resources, much as the Conference Board projects south of the border.

Standing in contrast to these demand pressures is the federal objective as outlined at our last meeting, to reduce federal program expenditures by 1990/91 to a smaller proportion of GNP than at any time since 1961. Let us remember that in 1961 there was no Medicare system and a much smaller post-secondary education system. Telling Canadians that federal transfers to provinces for health and post-secondary education will be cut proportionately with other federal expenditures does not engender confidence for the future of these important services.

We cannot meet Canadian health needs, including those of the rapidly increasing numbers of pensioners, without increased resources.

If Ottawa is not prepared to be a full and equal partner with the provinces in financing health care or turns its back on the increasing requirements our society faces, we will simply not be able to preserve Medicare.

I believe provinces would attempt to carry the extra burden either through increased taxes or through deficits. The poorer provinces would soon find that the tax levels necessary to compensate for federal cuts were undercutting their ability to maintain reasonably competitive tax structures, a necessary requirement for regional economic development. There would be irresistible pressure to slow expenditure growth by lowering program standards, comprehensiveness and accessibility.

Citizens who can afford it will offset these reduced quality factors through increased private sector delivery. Canadians would find themselves with a two-tier system of health care with unequal access, expensive duplication of services, and cost increases in aggregate far exceeding those of maintaining a comprehensive public health care system.

In 1982, according to Statistics Canada, the wealthiest 12% of families spent on average five times the amount the poorest 14% of families managed to spend on health care. The bottom quarter only spent one-third the amount of the top quarter. I have no doubt that without the universal, comprehensive Medicare program in place, the disparities inherent in these figures would be even more dramatic.

In Canada we need not and must not allow health care, treatment of illness, even life and death itself to become dependent on personal wealth. We must not return to the Russian roulette kind of financing which characterized pre-Medicare days in Canada.

The future of higher education in Canada is subject to similar pressures. There is increasing demand for full access to first rate post-secondary education opportunities, opportunities all the more important in the face of increasing technology and requirements for improved skills. I believe our people have a right to demand that those opportunities be preserved and enhanced. Cuts in the federal commitment would be a retrograde step and diminish our ability to provide those opportunities.

In Ottawa today, the federal government proposed major cuts in federal direct purchases of training spaces in our community colleges, cuts of 10% in 1986, a further 15% in 1987 and a further 20% in 1988. Notwithstanding federal suggestions that employers will utilize the colleges for training under the Canadian Jobs Strategy, serious concern remains with the impact the cuts may have on community colleges and more seriously on ordinary Canadians seeking upgraded skills.

Some may feel that the equalization program provides protection for less wealthy provinces, protection which could be used to offset the deleterious effects of reducing federal commitments to the financing partnership for health and post-secondary education. However, that argument does not stand up to scrutiny.

As we all know, the equalization program does not even bring recipient provinces' ability to raise revenues to the all-province national average. That means recipient provinces will simply be unable to compensate for federal cuts. That, in turn, would run strongly counter to the constitutional commitment to equalization:

> "That provincial governments have sufficient revenues to provide reasonably comparable public services at reasonably comparable levels of taxation."

Conclusion

In August, the Premiers of Canada informed the federal government that they "rejected" the cuts in federal transfers proposed in the May federal Budget. I would like to quote from their communique:

> "[Premiers] noted the projected increasing demands on the health care system as the proportion of elderly Canadians continues to increase in coming decades and the increased pressure on our post-secondary education system for improved education and increased skills. Federal and provincial governments must work cooperatively and effectively to ensure these needs are met."

The ten premiers went on to say:

> "The federal government has an important role to play, through the Established Programs Financing Arrangements, in sustaining health and post-secondary service throughout the country. Federal cutbacks, as proposed in the May Budget, are clearly inconsistent with maintaining present levels of service, let alone meeting projected needs."

I believe the Premiers are right in their assessment.

Canadians should not be asked to support a reduction in the level of public services in the vital health and post-secondary education areas, with the attendant substitution of access to private sector alternatives only for the rich. That would be socially unjust and violate a "sacred trust."

By international standards, Canada, with federal-provincial cooperation and partnership, is already "spending smarter" than could be achieved through private schemes. The major advantages and benefits of our Canadian system must be maintained. It is worth sacrificing to do so just as our parents sacrificed to provide these services for us.

To preserve these programs, Ottawa must again become an equal partner with the provinces in maintaining our public health and post-secondary education systems. In Manitoba's view, a 50:50 partnership between federal and provincial governments is a fair deal and one worth fighting for.

BACKGROUND ON THE FEDERAL-PROVINCIAL ARRANGEMENTS FOR FINANCING HEALTH AND POST-SECONDARY EDUCATION

Prepared By The
Department of Finance
Government of Manitoba

November, 1985

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BACKGROUND ON THE FEDERAL-PROVINCIAL ARRANGEMENTS FOR FINANCING HEALTH AND POST-SECONDARY EDUCATION

INTRODUCTION

Federal financial support for provincial health and post-secondary education programs is provided through the Established Programs Financing Arrangements (EPF). The importance of these arrangements is underscored by two simple facts:

1. Expenditures on Health and Post-Secondary Education are large and rapidly growing. Within the ten provinces, some $33.9 billion was devoted to these functions in 1984/85, an amount equivalent to $1,293 per capita.

2. Established Programs Financing is the largest federal transfer to provinces. Federal cash payments amounted to $8.2 billion in 1984/85. The tax transfer and associated equalization was worth an additional $6.4 billion. The federal share of total health and post-secondary spending is 43.0%.

To Canadian citizens, the importance of EPF lies not in the apportioning of costs between the two orders of government, but rather in the fact that it has provided the firm and stable financial foundation on which this nation has built its first rate health care and post-secondary education systems.

Provincial Ministers have, over the years, defended the basic principles of the arrangements while raising issues of adequacy, stability and flexibility. At their recent Conference, Canada's Premiers referred to the increasing demands on the health care and post-secondary education systems and stated "federal and provincial governments must work cooperatively and effectively to ensure these needs are met."

In 1981 and again in 1983, provincial Ministers of Finance and Treasurers prepared reports on these programs and on the Established Programs Financing Arrangements. Data has again been compiled by provinces and made available to the federal Department of Finance, in order to provide a complete perspective to the financing arrangements for health and post-secondary education. The statistics presented in Appendix A of this document are drawn from that data base.

BACKGROUND

Shared-Cost Arrangements

Until 1977 health and higher education in Canada were financed under cost-shared arrangements.

Under cost-sharing, federal participation in these vital services took the form of 50/50 cost-sharing of "eligible" costs. Experience with the shared-cost arrangements revealed a number of important weaknesses.

Over time, federal and provincial governments became increasingly concerned that the rigidities of the cost-sharing arrangements were resulting in inappropriate allocations of scarce resources towards higher cost options simply because the costs were shareable rather than towards more economical and efficient alternatives which were not eligible for cost-sharing. For example, certain low-cost alternatives to hospitalization such as nursing homes and home care were not eligible for cost-sharing.

A second weakness lay in the perceived lack of adequate controllability and predictability of the contributions in the federal Budget. This lead to various federal restrictions and caps on the federal commitment to health and higher education which resulted in erosion of the federal share and uncertainty as to the longer term stability and adequacy of federal support.

The Origins of Established Programs Financing

In moving towards the Established Programs Financing block funding arrangements, the federal government set out five principles which it believed should govern the new arrangements. Of particular importance were the following three:

- Adequacy - the federal government should continue to pay a substantial share of program costs;
- Flexibility - federal payments should be calculated independently of provincial program expenditures; and
- Stability - the arrangements for the "mature" programs should be placed on a more permanent footing.

Under the new Established Programs Financing Arrangements which came into effect April 1, 1977, federal cost-sharing for provincial hospital insurance, medicare and post-secondary education programs was replaced by a formula-determined transfer of cash payments and greater income tax responsibility to provinces. The amount of the overall transfer was established in relation to provincial cost-sharing receipts in 1975/76 on a per capita basis.* This amount was to be increased each

*"Base" cash and tax transfer figures were calculated for 1975/76 each roughly equal to one-half total federal contributions to the health insurance and post-secondary education programs. The tax transfer comprised 13.5 percentage points of personal income tax and 1 percentage point of corporation income tax.

year in relation to a three-year moving average growth in Gross National Product. In this manner, both orders of Government were assured reasonable stability and predictability of federal funding. Moreover, because transfers were no longer tied to federally-determined definitions of eligible spending, "penalties" against more effective utilization of available resources as existed under cost-sharing were removed.

Changes Since 1977

Despite objections, a number of significant changes to the Established Programs Financing Arrangements have been implemented since 1977 to reduce the federal commitments. These changes included a reduction in overall Established Programs Financing transfers equal to the value of 2 personal income tax points commencing April 1, 1982. Subsequently, the former federal government capped the growth of federal contributions ostensibly related to post-secondary education in 1983/84 and 1984/85 to 6% and 5%, respectively. In combination, these changes have reduced overall federal Established Programs Financing support by 8.0% (or an estimated $1.3 billion annually in 1984/85) compared with the original arrangements.

CURRENT CONCERNS

Those federal actions rekindled longer-term concerns, concerns which in many cases had been anticipated prior to the inception of the Established Programs Financing Arrangements.

Adequacy

The major concern with respect to Established Programs Financing has been the adequacy of tieing federal support to growth in the Gross National Product. Under the Established Programs Financing system with federal contributions determined independently from program costs, the federal government no longer shares in the financial risks associated with increasing cost pressures and program needs in health and post-secondary education programming. Equally, Ottawa no longer shares in the rewards should the provinces manage to meet program needs with spending growth lower than GNP. However, since 1979, program costs and needs have grown faster than GNP, increasing their share of GNP particularly during the recession, while actions by the former federal government eroded the federal commitment. By 1984/85, overall federal support fell some $2.4 billion short of 50/50 sharing of total spending.

The adequacy of the current EPF Arrangements to meet present and future needs remains a serious concern. As stated in the 1985 Premiers' Conference Communique on Federal-Provincial Fiscal Relations:

> "[Premiers] noted the projected increasing demands on the health care system as the proportion of elderly Canadians continues to increase in coming decades and the increased pressure on our post-secondary education system for improved education and increased skills. Federal and provincial governments must work cooperatively and effectively to ensure these needs are met."

Stability

The utilization of an escalator based on a three-year moving average of GNP can provide a welcome measure of stability to federal support for health and post-secondary education. The three-year moving average avoids the wide and disruptive swings in federal support which would occur under a year-by-year escalator. In particular, during periods of slow growth or recession, the federal contribution will hold up. Similarly, federal costs will be less volatile in years of strong economic performance.

Unilateral federal actions in the past to reduce the federal contribution have threatened this very important feature of the arrangements. Provinces are hopeful that in the true spirit of renewed federal-provincial cooperation, appreciably greater stability will be provided in future than has been the case since 1982.

As the Premiers' Conference communique stated:

> "The federal government has an important role to play, through the Established Programs Financing Arrangements, in sustaining health and post-secondary service throughout the country. Federal cutbacks, as proposed in the May Budget, are clearly inconsistent with maintaining present levels of service, let alone meeting projected needs."

Flexibility

Another area of controversy under Established Programs Financing has been the federal government's arbitrary allocation of the block fund into separate health and post-secondary education components. Such allocations were never discussed with the provinces when Established Programs Financing was introduced. Indeed, the flexibility on the part of provinces to move funding between program areas in accord with local priorities and needs was seen as a major benefit when block-funding was introduced. In particular, it was generally accepted that there would be a longer term shifting of resources in favour of health programming relative to post-secondary education.

Unfortunately, the use of arbitrary allocations based on the split of federal contributions in 1975/76 under the former cost-sharing arrangements was extended and formalized by Bill C-12 in 1984 (a Bill opposed by both the Progressive Conservative and New Democratic Parties). This has given rise to significant misconceptions and misunderstanding. For example, the Johnson Report on Post-Secondary Education accepted the federal procedure and overallocated the Established Programs Financing block fund to post-secondary education*, underestimated spending on post-secondary education in the provinces and suggested that the federal contribution ranged from 60% to 107%! While such arbitrary allocations if pursued, imply an analogous federal share of health program costs at 40%, on average, that fact was simply ignored in the Johnson Report. Not surprisingly, such unbalanced presentations have created confusion, not only about the sharing of costs, but also about the future funding levels and arrangements for this sector.

Provinces believe the segmented approach and arbitrary splitting of the Established Programs Financing block fund is inappropriate, both because it fuels perceptions of provincial underfunding of post-secondary education and because it suggests that the federal contribution is significantly more generous than it truly is.

CONCLUSION

In light of the importance of our health and post-secondary education systems to all Canadians, Established Programs Financing Arrangements must be reviewed thoroughly and improved to ensure adequate, stable and predictable funding.

*Some 32.1% of the Established Programs Financing Fund was allocated to post-secondary education and the remaining 67.9% to health care. In contrast, spending patterns throughout Canada currently entail roughly 25% on post-secondary education and 75% on health care.

SUMMARY OF TABLES

The federal cash contribution declined over the first five years of the Established Programs Financing Arrangements from 26.7% of spending in 1977/78 to 24.2% in 1981/82 and has stabilized at that level through 1984/85. Adding in the tax portion associated with Established Programs Financing transfers, the federal input would be calculated as declining from 48.7% in 1977/78 to 46.7% in 1981/82 and stabilizing at about 43% since.

If federal contributions to health and post-secondary education were allocated on the same basis as program spending, the federal share for each would be the same as for the totals noted above. However, using the artificial allocation by program which has now found its way into such studies as the Johnson Report, the federal share of health spending has dropped from 46.7% in the first year of the Established Programs Financing Arrangements (1977/78) to 43.9% in 1981/82 and 40.4% in 1984/85. Under this formulation, federal post-secondary education funding has at the same time remained relatively constant, at 54.1% in 1977/78, 54.9% in 1981/82 and 51.5% in 1984/85. However, provinces do not accept this kind of allocation of the block fund (67.9% to health and 32.1% to post-secondary education before post-secondary education capping effects). Such an allocation is inconsistent with the fact that health programming encompassed 70.7% of total Established Programs Financing related expenditure in 1975/76 and 75.9% in 1984/85.

The data are presented in Appendix A.

APPENDIX A

ESTABLISHED PROGRAMS FINANCING
DATA SUMMARIES

TABLE 1

FEDERAL SHARE OF HEALTH AND POST-SECONDARY EDUCATION FINANCING

($ Million)

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85*
Federal Contributions for Health and Post-Secondary Education:								
Cash Plus Tax	7,273	8,207	9,257	10,430	11,743	12,363	13,532	14,572
Cash Only	3,985	4,485	5,002	5,458	6,095	6,433	7,527	8,209
Provincial-Local Government Health and Institutional Post-Secondary Education Spending**	14,943	16,533	18,542	21,335	25,139	29,026	31,744	33,855
Federal Share (Per Cent):								
Cash Plus Tax	48.7	49.6	49.9	48.9	46.7	42.6	42.6	43.0
Cash Only	26.7	27.1	27.0	25.6	24.2	22.2	23.7	24.2

*Reflects Canada Health Act penalties.
**Operating and capital expenditure.

TABLE 2

FEDERAL SHARE OF HEALTH FINANCING
($ Million)

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85*
Federal Contributions for Health								
Based on Artificial Federal Split**	5,086	5,737	6,470	7,288	8,205	8,657	9,564	10,365
Based on Spending Ratios as Shown in Table 4	5,302	6,016	6,758	7,708	8,737	9,260	10,203	11,060
Provincial-Local Government Health Spending***	10,900	12,120	13,538	15,767	18,693	21,746	23,924	25,685
Federal Share (Per Cent)								
Artificial Split**	46.7	47.3	47.8	46.2	43.9	39.8	40.0	40.4
Split on Spending Ratio	48.7	49.6	49.9	48.9	46.7	42.6	42.6	43.0

*Reflects Canada Health Act Penalties.
**Using artificial split of E.P.F. which allocates 32.1% to P.S.E. and 67.9% to health, a view rejected by all provinces.
***Operating and capital expenditure.

TABLE 3

FEDERAL SHARE OF POST-SECONDARY EDUCATION FINANCING
($ Million)

	1977-78	1978-79	1979-80	1980-81	1981-82	1982-83	1983-84	1984-85
Federal Contributions for Post-Secondary Education								
Based on Artificial Federal Split*	2,187	2,470	2,788	3,142	3,538	3,705	3,968	4,207
Based on Spending Ratios as Shown in Table 4	1,971	2,191	2,499	2,722	3,006	3,103	3,329	3,512
Institutional Post-Secondary Education Spending**	4,043	4,413	5,005	5,568	6,446	7,280	7,820	8,170
Federal Share (Per Cent)								
Artificial Split*	54.1	56.0	55.7	56.4	54.9	50.9	50.7	51.5
Split on Spending Ratio	48.7	49.6	49.9	48.9	46.7	42.6	42.6	43.0

*Using artificial split of E.P.F. which allocates 32.1% to P.S.E. and 67.9% to health, a view rejected by all provinces.
**Operating and capital.

TABLE 4

PROVINCIAL HEALTH AND POST-SECONDARY EDUCATION SPENDING RATIOS
(%)

	Health	Post-Secondary Education
1975-76*	70.7	29.3
1976-77	70.9	29.1
1977-78	72.9	27.1
1978-79	73.3	26.7
1979-80	73.0	27.0
1980-81	73.9	26.1
1981-82	74.4	25.6
1982-83	74.9	25.1
1983-84	75.4	24.6
1984-85	75.9	24.1

*Note that even in 1975-76 the spending ratio among programs differs from the ratio used by the former federal government to split E.P.F. of 67.9/32.1. The latter ratio relates to the time when a considerable portion of provincial health spending was not eligible for federal cost-sharing.

TABLE 5

FEDERAL SHARE OF MANITOBA EXPENDITURES

$ Millions

	1977/78	1978/79	1979/80	1980/81	1981/82	1982/83	1983/84	1984/85
Federal Contributions for Health and Post-Secondary Education								
Cash & Tax	315.0	358.0	400.4	441.5	491.1	520.7	567.6	618.0
Cash Only	194.8	222.2	247.7	266.1	293.3	315.0	357.0	395.3
Provincial-Local Government Health and Post-Secondary Education Institutional Spending (Operating & Capital)	644.5	667.2	742.1	851.3	1,027.3	1,191.3	1,334.2	1,428.5
FEDERAL SHARES (Per Cent):								
CASH & TAX								
MANITOBA	**48.9**	**53.7**	**54.0**	**51.9**	**47.8**	**43.7**	**42.5**	**43.3**
All Provinces (estimated)	48.7	49.6	50.0	48.6	46.7	42.6	42.6	43.0
CASH ONLY:								
MANITOBA	**30.2**	**33.3**	**33.4**	**31.3**	**28.6**	**26.4**	**26.8**	**27.7**
All Provinces (estimated)	26.7	27.1	27.0	25.6	24.2	22.2	23.7	24.2

APPENDIX B

PROVINCIAL PREMIERS' COMMUNIQUES

26th Annual Premiers' Conference St. John's, Newfoundland

COMMUNIQUE ON FEDERAL-PROVINCIAL FISCAL RELATIONS

The ten provincial Premiers rejected the proposal in the May Federal Budget to cut federal support for health and post-secondary education and national equalization by some $2 billion annually by 1990. They agreed that attempts to shift the federal deficit on to the backs of the people will not help the Canadian economy. Both orders of government serve the same taxpayers and offloading responsibilities and costs from one order to the other will not help in meeting service needs.

They noted the projected increasing demands on the health care system as the proportion of elderly Canadians continues to increase in coming decades and the increased pressure on our post-secondary education system for improved education and increased skills. Federal and provincial governments must work cooperatively and effectively to ensure these needs are met.

The federal government has an important role to play, through the Established Programs Financing arrangements, in sustaining health and post-secondary service throughout the country. Federal cutbacks, as proposed in the May Budget, are clearly inconsistent with maintaining present levels of service, let alone meeting projected needs.

The Premiers also recognize the importance of these and other federal transfers as well as direct federal activity to sustaining their shared goal of fair and balanced regional development.

The National Equalization Program is of fundamental importance to Canadian Confederation. Premiers stressed the urgent need to place equalization on a sound foundation. This is essential to fulfill the constitutionally enshrined objective of the program.

The Premiers suggested that Finance Ministers should coordinate the federal provincial review of these arrangements. They noted that federal and provincial Finance Ministers will be meeting to discuss the federal cutback threat in September. The Premiers requested their Finance Ministers to report to them on the results of that meeting prior to the Halifax First Ministers' Conference.

Western Premiers' Conference: Grande Prairie, Alberta May 13-15, 1985

Communique #6

FEDERAL-PROVINCIAL COOPERATION

Western Premiers agreed today that a high degree of prior consultation among the federal and provincial governments is necessary in order to ensure that discussions at the Annual First Ministers' Conference in November are productive. The important role that First Ministers' Conferences play in shaping national policy necessitates thorough pre-conference discussions. To ensure a successful conference, Western Premiers proposed that each government appoint a team of ministers to coordinate preparations.

Recognizing that federal and provincial governments serve the same taxpayers, the Western Premiers stressed that the federal government must not shift its deficit to the provinces through reductions in federal transfer payments.

They reaffirmed that Established Programs Financing is a block-funding arrangement for both health and post-secondary education. They rejected any attempt, as in the "Johnson Report" recently released by the federal government, to focus on artificially defined federal contributions to post-secondary education. The increasing provincial cost of maintaining health services makes this arbitrary separation even less tenable.

The Premiers recognized the need for federal and provincial governments to work cooperatively to ensure the stability, predictability and adequacy of federal contributions to health and post-secondary education programming. The review of Established Programs Financing, including any discussions on post-secondary education and health care, should be coordinated by federal and provincial Treasurers and Ministers of Finance.

The Premiers committed themselves to building upon the spirit of cooperation demonstrated at the February First Ministers' Conference in Regina.

APPENDIX C

PRINCIPLES UNDERLYING THE 1977 ESTABLISHED PROGRAMS FINANCING ARRANGEMENTS

When EPF arrangements were first proposed to the provinces at a First Ministers' Conference on June 14, 1976, the objectives of EPF were outlined by the Prime Minister at that time, as follows:

(1) "To maintain across Canada the standards of service to the public under these major programs, and to facilitate their improvement;

(2) "to put the programs on a more stable footing so that both levels of government are better able to plan their expenditures;

(3) "to give the provinces flexibility in the use of their own funds which they have been spending in these fields;

(4) "to bring about greater equality among the provinces with regard to the amount of federal funds they receive under the programs;

(5) "to provide for continuing joint policy discussions relating to the health and post-secondary education fields."

Mr. Trudeau went on to identify the principles underlying these objectives as the following:

(1) "The federal government should continue to pay a substantial share of program costs;

(2) "federal payments should be calculated independently of provincial program expenditures;

(3) "there should be greater equality in per capita terms among the provinces with regard to the amount of federal funds they receive under the programs;

(4) "the arrangements for these major programs should be placed on a more permanent footing;

(5) "there should be provision for continuing federal participation with the provinces in the consideration and development of policies of national significance in the fields of health and post-secondary education."

At a subsequent First Ministers' Conference, on December 13, 1976, the then Minister of National Health and Welfare, Mr. Lalonde, stated that, "The introduction of the Hospital Insurance and Medical Care programs into Established Programs Financing would have three very important results:

(1) "First, the movement to block-funding would increase substantially the flexibility available to provinces with regard to program decisions. At the same time, there would be a simplification of administrative procedures;

(2) "second, any savings that can be generated by reducing the services would accrue totally to the provinces and would not be shared by the Federal Government since our contribution under Established Programs would not be directly related to program costs;

(3) "third, all the projections suggest that the Established Programs formula being considered at this time would yield more resources to the provinces than a continuation of current arrangements for the health and post-secondary education programs."

APPENDIX D

RECENT STATEMENTS ON FEDERAL-PROVINCIAL FISCAL ARRANGEMENTS

HONOURABLE VICTOR SCHROEDER
MINISTER OF FINANCE
PROVINCE OF MANITOBA

NOTES FOR A STATEMENT
ON FEDERAL-PROVINCIAL FISCAL RELATIONS

FEDERAL-PROVINCIAL CONFERENCE OF
FINANCE MINISTERS AND PROVINCIAL TREASURERS

HALIFAX, NOVA SCOTIA
September 26-27, 1985

Just over one month ago, provincial Premiers discussed the cutbacks in federal support for health, post-secondary education and equalization programs proposed in the May federal Budget.

They rejected the proposals contained within the Budget and looked forward to this meeting of Finance Ministers to begin the dialogue necessary to overcome this threat to cherished national programs. A good place to begin is to establish the facts surrounding the issues under debate.

With respect to the Equalization Program, it is vitally important to keep in mind that the five-province standard currently falls nearly $250 per capita short of the all-province national average standard covering the same comprehensive and representative tax bases. In our view, that has serious implications on the ability of the current formula to meet the objective set out in our Constitution, that is, to ensure:

> "That provincial governments have sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation."

It also has an impact on the degree to which all equalization recipient provinces can provide adequate public services while holding their tax rates to levels competitive with the four richest provinces.

There is widespread dissatisfaction with the results of the current Equalization Program and the consequential resort to extensive ad hoc arrangements in efforts to obtain minimally acceptable results. That is why Premiers referred to the urgent need to "place equalization on a sound foundation" and pointed out that:

> "This is essential to fulfill the constitutionally enshrined objective of the program."

From a Manitoba perspective, we also must deal with the regional distortions introduced by the 1982 changes in equalization which, as noted by independent observers such as Thomas Courchene and the Macdonald Commission, have hit Manitoba most severely.

With respect to Established Programs Financing for health and post-secondary education, we have witnessed a continuing series of unfortunate presentations which by virtue of artificial, arbitrary and deficient statistics have created inaccurate and misleading conclusions. I refer specifically to the Johnson Report released by the Secretary of State and referenced in the Macdonald Report. And, I might note a similar arbitrary allocation of the EPF block fund appears to be incorporated in the Nielsen Task Force on post-secondary education. I look for assurances from the federal government that its decisions will not be based on such misleading information.

Over the past two decades, health spending has outpaced GNP growth in Canada, rising from about 6% to over 8% of GNP. In the United States, the trend has been sharply higher than in Canada. Now, as Premiers noted, there are increasing demands projected on the health care system as the proportion of elderly Canadians continues to increase in coming decades. All our Health Ministers know full well the implications on program costs of maintaining current services for the 31% increase in Canadians over 65 expected between 1981, when the former federal government proposed the 1982 arrangements, and 1991. Our Government is committed to doing everything we can to ensure quality health care remains available to all Canadians on a universal basis.

There is increased pressure on our post-secondary education system for improved education and increased skills. The Macdonald Commission and the Johnson Report have both proposed increased spending for training and research. Our Government believes it will be critical for federal and provincial governments to work cooperatively and effectively to ensure these needs are met.

As Premiers noted last month:

> "The federal government has an important role to play, through the Established Programs Financing arrangements, in sustaining health and post-secondary education services throughout the country."

Unfortunately, federal support in relation to health and post-secondary education costs has deteriorated significantly in the last several years from 50% in 1979/80 to 43% in 1984/85.

The significantly less than 50% federal share raises serious questions about the adequacy of the federal contribution. Against this backdrop as all ten Premiers affirmed:

> "Federal cutbacks, as proposed in the May Budget, are clearly inconsistent with maintaining present levels of service, let alone meeting projected needs."

In our discussions, we should all remember that any federal cutback in support to provinces will, of necessity, have consequences for the quality and accessibility of provincially-delivered programs, or alternatively for provincial taxes and/or deficits. This is especially so in those provinces whose fiscal capacity falls below the national average.

We understand that professed concern about the federal deficit plays a primary role in motivating the proposed cuts. However, these health and education programs improve the lives of all Canadians. They are solid investments in the future. Canadians deserve better than to have these fundamental services attacked.

Moreover, there are alternatives. For example, our Government has proposed comprehensive tax reform to close the loopholes and limit tax expenditures which benefit only narrow interests in our society. And, more and more ordinary Canadians are questioning the priorities of a national government which in the same Budget proposes tax cuts totalling $2.3 billion annually in 1990/91 for the wealthy (through capital gains exemptions and pension contribution deductions) and at the same time proposes $2 billion in cuts in federal support for health care and post-secondary education, and equalization to poorer provinces.

I look forward to learning more about the views of the federal government on these important matters. I earnestly hope that the federal government will join with the provinces in a sincere effort to not only protect but rather to strengthen these programs to the benefit of all Canadians.

St. John's
1985

DOCUMENT: 850-31/017

HONOURABLE HOWARD PAWLEY

PREMIER OF MANITOBA

NOTES FOR A STATEMENT

ON FEDERAL-PROVINCIAL FISCAL RELATIONS

1985 PREMIERS' CONFERENCE

ST. JOHN'S, NEWFOUNDLAND

AUGUST 20-22, 1985

Introduction -- A Commitment to Cooperative Federalism

Mr. Chairman:

I welcome the opportunity to lead off our discussions of federal-provincial fiscal relations.

Since our Government took office in 1981, we have made the commitment to cooperative federalism a top priority for Manitoba.

While applying that principle is never easy, our Government is convinced that much more can be achieved through cooperation, by working together, than by the confrontationist approach which marked federal-provincial relations under the previous administration in our Province.

Whether in pursuing the elusive goal of constitutional protection for the rights of our native people, or in developing cooperative economic undertakings which resulted, for example, in Manitoba signing the first comprehensive Economic and Regional Development Agreements (ERDA), or in speaking out strongly to secure fair treatment from governments in Ottawa, we have worked to establish, maintain and enhance the institutions, agreements, commitments and programs which bind our federation together.

There have been gains and setbacks, and items put "on hold".

But, throughout it all, it has become abundantly clear, if there were ever any doubt, that this country, our national federation, works best when there is a spirit of cooperation amongst its leaders, when there is dedication to the principles of cooperative federalism, and when there is full appreciation and consideration of the diversity among the regions of Canada.

The Conferences of Premiers provide a special opportunity because we bring together the essential understanding of our regions, and we can work to reconcile our views and interests and to provide valuable direction for concerted federal-provincial action.

We are at a time in the history of Canada which affords us a significant opportunity to move forward, to resolve problems, to cement our federal foundations and to build for the future.

Since we met last August, we have a new federal government elected on a platform which included a strong commitment to improving federal-provincial relations.

There have been opportunities to reassess positions into which governments had become frozen for some period of time. Now, the 5-year review of the major Fiscal Arrangements provides provincial and federal governments a further impetus to re-examine the existing mechanisms, to ensure they will have the capability over the longer term to achieve the purposes for which they were established.

Throughout our deliberations, I trust all governments, provincial as well as federal, will remember that we ultimately all serve the interests of men and women throughout the country. While some may characterize federal-provincial fiscal relations only as a matter of narrow interest to governments, we know they are much more than that. They provide the financial base on which many vital social and economic initiatives depend for their existence.

There is room for optimism, but obviously it must be tempered in view of the economic and political situations we currently find in our Canadian federation.

The Economy

Unemployment remains the number one problem facing our country.

According to the official statistics, some 1.3 million Canadians are unemployed today. For each nine working men and women, there is another unemployed Canadian actively searching for work. These figures do not include those whose prospects are so poor that he or she has abandoned the search. And, as we are all painfully aware, the problem is acute for young people seeking a first job, and particularly so for women and natives.

The new federal government campaigned on a platform of jobs, jobs, and more jobs. Throughout the election campaign, it expressed real concern for the jobless, it spoke of compassion and of a determination to act.

Yet, most forecasters have concluded that the measures introduced in the May federal Budget will actually cost Canadians jobs. For example, an analysis by the Conference Board suggests that the economy's capacity to generate employment will be seriously reduced, beginning in 1986, as a direct consequence of the Budget and that the negative impact on job creation is expected to grow over time.

According to the Conference Board assessment, by 1989 there will be some 280,000 fewer jobs available for Canadians than if the federal Budget measures had not been introduced. The Board also expects that the unemployment rate will be almost one percentage point higher.

That is a discouraging message for all of us. And, I am sure it is discouraging to the Prime Minister. But, that discouragement pales in comparison to the disappointed hopes and aspirations of unemployed Canadian men and women.

Last February in Regina, I said:

> "...the most important commitment we as First Ministers can make to Canadians is that the key objective of creating jobs and reducing unemployment will guide us in our deliberations."

I believe that is still the most important commitment we can make.

Mr. Chairman, I would like to turn now to some particular areas of evolving federal-provincial policy concern which affect people thoughout our country.

Nielsen Task Force

There is increasing concern that the recommendations emanating from the Nielsen Task Force are unduly hardening federal positions regarding program reductions, while often being ignorant of, or insensitive to the concerns of ordinary Canadians.

The ill-advised federal Budget proposal to de-index Old Age Pensions was one case in point. The leaked document on native people is another. Anxiety persists regarding the Task Force Review of the Canada Assistance Plan and other major program areas.

This ongoing concern is perhaps not surprising since the Program Review Process itself did not include provision for meaningful consultations with groups or with provinces which will be affected by its recommendations. As a result, it simply has not been sensitive to regional concerns or to the concerns of disadvantaged groups of Canadians, including native people.

I do not believe this lack of consultation to be at all consistent with the Prime Minister's stated desire for improved federal-provincial relations.

Manitoba has called for consultation on the activities of the Task Force -- not just staff discussions, but political discussions on directions, and objectives, and assumptions. I know other Premiers have made similar requests.

To my knowledge, however, there has been no federal commitment, yet, to Ministerial level consultation on Mr. Nielsen's work.

Economic and Regional Development

Sustained regional development initiatives are needed to build on the strengths of all parts of our country and to create jobs.

Certainly, the actions of individual provinces and of the federal government play important roles in assuring equitable and balanced development. There are obvious differences in development potential between provinces and also in their abilities to use that potential to the fullest.

National initiatives, including equalization and federal participation in the costs of programs of national scope, are therefore all the more important. Such national initiatives affect programs and services directly, and also affect each province's ability to maintain a tax structure that supports regional economic development.

Direct federal activity is also important to economic and regional development and perhaps of greater importance in the less advantaged regions.

Unfortunately, many of the decisions announced in the federal Economic Statement last November simply did not recognize the importance of federal activity to economic development. Many of the federal cut proposals entailed significant losses in jobs and activity throughout the country. The problems were particularly severe for Manitoba which, with 4.2% of Canada's population, was to bear over 7% of the proposed cuts and an associated loss of 6,000 jobs.

Our Government shared the disappointment of ordinary Canadians throughout the country that the May federal Budget contained no action to redress these effects. In fact, as noted earlier, the federal Budget is expected to add further to the unemployment problem rather than helping to resolve it.

As Premiers, we each recognize the importance of the Economic and Regional Development Agreements (ERDA's) to long-term economic development in each region. We also recognize the importance of governments proceeding to live up to their respective commitments under these agreements.

In Manitoba, we have had some problems with some individual federal Departments -- problems we hope are not symptomatic of a change in Ottawa's attitude to the ERDA system.

Fiscal Arrangements

The Federal-Provincial Fiscal Arrangements governing health and post-secondary education financing and equalization are of key importance to all Canadians. Though sometimes viewed only in the narrow context of transfers between governments, equalization has often been referred to as the "glue which holds our country together." It is critical to assuring reasonable comparability of important public programs in all regions of the country, and it is critical in the economic development prospects of the have-not provinces.

Established Programs Financing provides the necessary financial underpinnings to the quality health care and post-secondary education opportunities demanded and deserved by our citizens.

Equalization

Manitoba's experience with the current equalization formula continues to be unsatisfactory. Our Province's share of equalization has declined from 9.1% under the old formula in 1981/82 to 7.0% under the basic formula currently in place. Even with supplemental payments, **our Province faces actual cuts in equalization support from the 1984/85 total of some $22 million this year and $48 million next year.** These scheduled cuts in federal support are to occur despite a 10.5% increase in our Province's need for support as measured under the formula.

That pattern of increasing need and decreasing support has a profound impact on our efforts to maintain comparable quality programming, strengthen our economy and retain competitive tax rates. It will come as no surprise that our province shares the position of Quebec, and, we hope, of other provinces, on this matter -- that federal support simply should not be cut when need is increasing.

The need for a thorough review of the equalization formula is underscored by the experience since 1982. The extensive use of ad hoc arrangements, including the transitional arrangements which affected five of the six recipient provinces last year, supplemental payments which affect all recipient provinces this year, and special override provisions for Newfoundland and Nova Scotia, are all symptoms of the inadequacies and shortcomings of the present formula.

The basic problem with the current formula is its use of an inadequate standard. **The current five-province standard means that the revenue available to recipient provinces including equalization falls $250 per capita short of the all-province national average.** In turn, that gap has real implications for the ability of recipient provinces to provide adequate public services, maintain efforts to strengthen the regional economies and maintain competitive taxes.

The formula must be overhauled if it is to meet the basic objective of the program as stated in the Constitution, that is to ensure:

> "that provincial governments have sufficient revenues to provide reasonably comparable levels of public services at reasonably comparable levels of taxation."

In our view, that purpose can only be achieved under an equalization formula based on the all-province national average standard.

Health and Post-Secondary Education Financing

Federal health and post-secondary education funding has been subjected to continuing controversy, with spurious arguments that provinces weren't spending enough, then that they were spending too much and the programs were too costly, and then that provinces weren't directing their funding to appropriate purposes. Our health and post-secondary education programs, universally accessible and of the highest quality, are a most important part of our Canadian heritage. These programs, important to Canadians in every region, are dependent on a sustained national commitment, federal as well as provincial, to sharing fairly in their costs.

In Canada, we have built an excellent health care system which provides needed services at reasonable cost. Interestingly, when Medicare was introduced in the mid-60's, approximately the same proportion of GNP was devoted to health care in Canada as in the United States. However, by 1981, health costs in the U.S., with its largely private care system, exceeded Canada's by more than one-quarter. Health care spending represented 10% of GNP in the U.S. compared with a moderate 8% of GNP in Canada.

Certainly, our health care system is experiencing significant cost pressures. That should not be surprising to any of us. We can all expect the health care needs of our people to increase as the number of elderly Canadians increases in the coming decades. By the year 2020, it is projected that senior citizens will comprise double the present share of the population.

The pressures on the post-secondary education system for better education and training in the face of enrollment increases and for research are also very real and compelling.

In short, there is every reason to expect that the expenditures which are now financed under EPF arrangements will continue to grow in real terms over the foreseeable future. The Prime Minister has described these programs as "a sacred trust". I agree wholeheartedly. Of course, it will be essential for federal and provincial governments to provide adequate resources to fulfill that sacred trust.

It is unfortunate that the former federal government was not prepared to share equally in the costs of these vital programs. In Manitoba, for example, the federal share of costs has dropped from 54% in 1979/80 to under 45% this year. Currently, federal EPF cash and tax transfers fall some $84 million short of providing equal sharing in the costs of these vital programs in Manitoba.

I understand that Provincial Finance Ministers are now completing a comprehensive study of provincial and federal financing of health and post-secondary education programs -- updating an earlier review conducted in 1983. Once Finance Ministers have completed that interprovincial overview, I would support making it public in order to provide a better basis for the discussion of future EPF funding.

Our Government believes that both the federal government and each provincial government must operate in the true spirit of cooperative federalism to protect these programs for Canadians. The new EPF arrangements must recognize the cost pressures within these programs, and the federal government should agree to provide an equal share of the costs. Without such a fiscal regime in place, Canada courts the danger of undermining two of the most important services provided to our people.

I might add that, in recognition of the block funding nature of EPF, it will remain important that discussions and negotiations be coordinated by our Finance Ministers.

Federal Transfer Payment Cuts

With the election of the new federal government, I shared the optimism of some of my colleagues that action would be taken to restore at least equal federal sharing in the costs of these programs.

We were, therefore, dismayed at the announcement of massive funding cuts proposed in the May federal Budget.

In our view, the proposal to cut federal support for equalization to have-not provinces and for health and post-secondary education from already depressed levels by $2 billion annually by 1990-91 is ill conceived, unjustified and inconsistent with earlier promises. Premiers are also aware that these transfers have fallen from close to 20% of federal program spending in 1981/82 to 18.0% in the May federal Budget. As a proportion of total spending, these transfers have fallen from 15.1% to 13.6% over the same period.

As Premiers, we must cooperate to persuade the federal government not to pursue such a proposed cut. Instead, we must persuade Ottawa to move toward at least equal sharing in the costs of vital health and education programming, and towards a fair equalization system based on the all-province national average standard.

Tax Reform

At last year's Premiers' Conference in Charlottetown and again at the First Ministers' Conference in Regina, Manitoba stood alone in raising the tax reform issue. I am pleased to note that since then Saskatchewan has joined us in pushing for national tax reform and, at Grande Prairie in May, all four Western Provinces endorsed a communique calling for national tax reform.

The case for reform is strong. It arises from the myriad of incentives, preferential provisions and loopholes now contained in our tax system. The magnitude of the abuses is such that numerous wealthy Canadians and profitable corporations are able to avoid paying any taxes, and growing numbers of Canadians believe the system is unfair.

In 1962, the then Prime Minister, the Right Hon. John Diefenbaker, established a Royal Commission, chaired by Mr. Kenneth Carter to study Canada's system of taxation. The 1966 Report of the Commission described the objectives of a nation's tax system:

> "The first and most essential purpose of taxation is to share the burden of the state

> fairly among all individuals and families. Unless the allocation of the burden is generally accepted as fair, the social and political fabric of a country is weakened and can be destroyed."

It has become increasingly apparent that, by these standards, Canada's income tax system is failing miserably.

1) Income taxes have become increasingly unfair and inequitable. Our Government has always endorsed the position of the Carter Commission that taxes should reflect ability-to-pay. As the Commission expressed it:

> "All resident individuals and families should pay taxes on a base that measures the value of the annual net gain or loss in the unit's power, whether exercised or not, to consume goods and services. Such a base would ignore the form of the gain or what was done to obtain the gain. We call this the comprehensive tax base."

In fact, this principle often referred to as "a buck is a buck" is grossly violated in the present system. In 1983, for example, over 85% of labour income was assessed for tax purposes. In contrast, less than 45% of investment income entered the tax base in that year. Clearly, ordinary, working Canadians are paying more than their fair share.

2) The income tax system has not generated the revenues required to finance essential public services. Programs for ordinary Canadians have been slashed and taxes which are not related to income have been steadily increased. As a result, lower and moderate income Canadians, both working and retired, have been confronted with:

- an increasingly inequitable share of income taxes;
- increasing reliance on taxes that are inherently less progressive than the personal income tax; and
- cuts in important public services.

The serious nature of the problem was underscored earlier this year when, despite an improving

economic situation, Ottawa adjusted its estimates of the yield of personal income taxes down significantly, raising uncertainty about the ability of the income tax system to raise revenues.

More recently, federal analysis has confirmed the connection between declining income tax revenue productivity and the deficits facing governments throughout Canada. I quote:

> "(The) drop in the rate of growth of personal income tax revenues has been a major concern and is one of the primary reasons underlying the rapid increase in the federal government's deficit over these two years (1983 and 1984)."

Clearly, if senior governments do not act on tax reform, even greater pressure will be placed on public programs and services.

In our view, the tax package contained in the May federal Budget represents a significant step in the wrong direction. Certainly, it cannot be regarded as a reasonable approach towards meaningful tax reform.

On the personal side, major tax cuts are provided for the wealthy through the $1/2 million capital gains exemption and the increases in tax deductible pension contributions for higher income earners. Clearly, these cuts, entailing an annual cost of $2.3 billion annually by 1990/91, for the more fortunate are not helping to reduce the federal deficit, nor are they helping secure the resources needed for important public services.

On the corporate side, the Budget proposed new measures to permit transfers of tax losses, largely unused tax incentives and deductions, within corporate groups. The proposal will result in significant revenue losses federally ($400 million annually) and unspecified losses provincially.

In a separate discussion paper on corporate income taxes, the federal government identified major tax preferences which should be examined in the interests of providing a more fair and rational corporate income tax base. These included accelerated capital cost allowances in excess of actual depreciation, preferential tax rates, resource write-offs, the investment tax credits, and the inventory valuation allowance.

Our Government fully supports a comprehensive review of the corporate income tax base. Moreover, in our view, it is important that this review be completed and the existing corporate tax system cleaned up before considering any broadening of the transferability of unused tax deductions and preferences among corporations.

Our Government has long felt than an objective review of the corporate tax system would confirm that many preferences have either outlived their usefulness or are not effective. In our view, those provisions should simply be rescinded with the bulk of the resulting revenues used to help provide a more secure base for important public services and to increase federal fiscal flexibility.

It was therefore particularly disturbing to hear the federal government suggest that rationalization of the corporate tax base not be used to help protect vital public services in Canada, not be used to help reduce taxes on ordinary Canadians, and not be used to help reduce deficits. Instead, the federal Minister of Finance has suggested that any rationalization of the corporate tax base be accompanied by offsetting general federal corporate rate reductions with a view to ensuring that the overall effect of changes is "revenue-neutral."

Our Government does not believe that suggestion to be appropriate or fair, particularly at a time when the federal government, on the basis of concern over its own fiscal flexibility, proposed cuts in Old Age Pensions, cuts in social and economic programming, and cuts in its support for health, education and equalization throughout the country.

I ask all Premiers to join in urging the federal government to undertake a broadly based, intensive, National Tax Reform Conference. Such a Conference, which should include not only provincial governments, but also Canadians from all walks of life, would be the first step towards a truly meaningful consultation process.

The costs of allowing tax policy to be formulated in the bowels of federal Finance, accessible only to corporate tax planners, are obvious. Clearly, the time has come to open this important function of government to all Canadians.

Conclusion

Earlier, I talked about the importance of federal-provincial relations and these Conferences to ordinary Canadians, to vital health, education and social programming and to equitable and balanced regional development. I also emphasized some key concerns:

- The primary national issue facing us is the continuation of unacceptably high unemployment. There should be no disagreement on that. Provincial and federal governments must therefore pursue appropriate strategies to improve job prospects across this nation.

- Equalization, other federal transfers and direct federal activity are all important to sustaining regional development. Care must be taken to ensure that the regional dimensions are reflected fairly in federal decisions.

- The Equalization Program itself must be placed on a sound foundation, related to a national standard, and incorporating a measure of revenue stability if it is to fulfill its constitutionally enshrined objective. As a matter of principle, equalization support to a province should not be cut while its need is increasing.

- The Established Programs Financing Arrangements for sustaining important Health and Post-Secondary Education programs should provide fair and equal cost-sharing between federal and provincial governments. In addition, these arrangements must recognize the unavoidable cost pressures associated with maintaining both quality and universal accessibility for all Canadians.

- The income tax system must be reformed to restore fairness and ensure it generates revenue sufficient to finance essential public services. The incentives, preferential provisions and loopholes introduced for various purposes have made the system increasingly unfair and inequitable and less capable of generating necessary revenue. As a result, vital public services cherished by men

and women throughout the country have been put in jeopardy. A national Tax Reform Conference should be held at the earliest possible opportunity to begin addressing this important and fundamental issue.

Every one of these concerns can, and must be resolved -- in fact, they can only be resolved -- through real federal-provincial cooperation.

Once again, I believe we must remind our federal colleagues and partners of that fact.

Thank you.

MANITOBA

MINISTER OF FINANCE

WINNIPEG
R3C 0V8

Honourable Michael Wilson
Minister of Finance
Government of Canada
Place Bell Canada.
160 Elgin Street
OTTAWA, Ontario
K1A 0G5

Dear Mr. Wilson:

With your letter dated April 4, 1985, you enclosed a copy of the Johnson Report on Post-Secondary Education and invited comments.

I must, at the outset, express some disappointment that your government chose to release the Report without providing provinces with any pre-publication opportunity for federal-provincial consultations to ensure a reasonably accurate portrayal of the Established Programs Financing Arrangements and the public services those arrangements help finance, health and post-secondary education. I note that federal Ministers have taken every opportunity to distance the federal government from the Report by referring to it as "a personal report." However, its release and subsequent federal comments suggest that it could become a focal point for federal-provincial discussions. Also, unfortunately, in the absence of specific comments by either level of governments, the Report appears almost by default to be becoming accepted as "factual" information which, of course, it isn't.

As you know, the Established Programs Financing Arrangements began in 1977 as a block funding mechanism for health and post-secondary education services. Unfortunately, over the succeeding years, the former federal government seemed bent more on minimizing and constraining its contribution to health and post-secondary education programming throughout the country than on ensuring stability, predictability and adequacy in federal funding.

First, there was the unilateral cutting of the EPF block fund by Mr. MacEachen in 1982, rationalized by the former federal government as eliminating the so-called revenue guarantee component of Established Programs Financing.

Then, in 1983, the federal government placed artificial caps on portions of EPF. You will recall that the former government sought to justify those caps as applying to what it viewed to be a post-secondary component of the Established Programs Financing block fund.

All ten provinces, and I believe your Party, opposed that approach as being artificial, unjustified and unrealistic. Nonetheless, it was imposed unilaterally by the federal Liberals.

Over time, the former federal government sought to use the artificial allocation of the EPF block fund to justify efforts to further undercut its support for vital health and post-secondary education programming. Essentially, this generally took the form of over-allocating the EPF block to post-secondary education and then focussing on the federal contribution to post-secondary education as being over 50% and "too high" -- with a persistent federal refusal to discuss and analagous federal share of health program costs at well under 50% and too low.

That kind of cynical approach to the financing of these important services for Canadians was one of the major factors poisoning federal-provincial relations.

With the election of your government, all provinces looked forward to a rekindled commitment to cooperative federalism.

Unfortunately, the Johnson Report on post-secondary education, perhaps not surprisingly, as Mr. Johnson was appointed by the former federal government, reverts to past practice of statistical manipulations for self-serving purposes. The Report purports to contain "facts" which are constructed so as to leave very serious mistaken impressions.

As an illustration of the serious factual errors in the Johnson Report, I would refer you to the 1983 Provincial Consensus Statement on EPF which indicated that the federal share of health and post-secondary education spending in 1977/78 amounted to about 26.6% on the cash side. The provincial report also indicated that the federal share might rise to as much as 48.6% in the event that the income taxes transfered to the provinces under the EPF arrangements were counted as part of the federal contribution rather than part of the general revenues raised by provinces to meet the costs of health and post-secondary education financing. By 1982-83, the federal share had dropped to 21.3% on a cash basis and to 42.4% if the approximately one quarter of provincial income taxes identified as an "EPF Transfer" were counted as a federal contribution.

Contrasted against the 1983 Provincial Consensus Statement, the Johnson Report fails on a number of different counts.

- First, it purports to break up the EPF block funding into post-secondary and health components. Provinces have never agreed to such a break-down pointing out that only by examining the entire EPF block and related programming can the full EPF picture be developed.

- Secondly, it counts too much of the EPF block fund as post-secondary education -- roughly one-third compared with the one-quarter/three-quarter split in provincial spending.

- Thirdly, it dramatically understates the program costs of post-secondary education in Canada. For example, for 1977-78, the Johnson Report suggests that the costs of post-secondary education Canada-wide were $2.9 billion. In contrast, as the 1983 Provincial Consensus Report noted, institutional post-secondary education expenditures amounted to $4.1 billion in that year. Factors missed by the Johnson Report include senior matriculation, capital spending, etc.

- Fourthly, the Report totally ignores the implications the misallocation of the EPF block to post-secondary education has for health financing.

From a Manitoba perspective, I might add that, using the one-third, two-third allocation embedded in the Johnson Report, EPF Cash in 1984/85 provides 26.7% of health expenditures, 30.7% of PSE expenditures for a total combined share of 27.7%. Adding in the "tax transfer" would raise the EPF share to 40.7%, 51.3% and 43.3%, respectively. Each of the latter figures are down over 10 percentage points since 1979/80 when the EPF shares (cash and tax) were 51.2% for health, 61.5% for post-secondary education and 54.0% for the combined total. The effects of past federal actions which have had the effect of shifting an additional 10% of the burden to Manitoba over a six year period (and probably resulted in similar shifts in other provinces), must be borne in mind when we begin our dialogue on the new arrangements.

I would also like to take this opportunity to review briefly some of the principles which I believe must guide the review of EPF:

- EPF is a block fund. Federal input through EPF to post-secondary education cannot be divorced from the share the federal government provides for the total of health and post-secondary expenditure.

- Phoney arithmetic which artificially splits the payments or redefines and limits the program costs which are being shared through EPF will not be helpful for our review and discussions on EPF. The broadest view must be taken as we begin our dialogue.

- Consensus should be vigorously pursued and unilateral action should be avoided.

- The appropriateness and adequacy of federal funding in EPF are essential concerns of federal and provincial Finance Ministers. Given the integrated nature of the EPF Arrangements, segregated discussions by program Ministers are unlikely to be successful.

- Stability and predictability of funding are major concerns.

We must begin the next round of consultations on fiscal arrangements in an atmosphere which leaves the stale taste of the past behind us. To me, the Johnson Report reiterated many of the Liberal's misuses of information and statistics. We will need a more complete portrayal of the situation to guide our decisions.

We have the Johnson Report. We will consider the information presented. I would recommend that it not become a focal point or agenda item for our future meetings on EPF arrangements.

Yours sincerely,

Vic Schroeder,
Minister of Finance.

c.c. Honourable M. Hemphill,
Dr. R.J. Duhamel.

All Provincial Ministers of Finance.

POOR
QUALITY
ORIGINAL